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BEFORE
THE PUBLIC SERVICE COMMISSION OF
SOUTH CAROLINA
DOCKET NO. 90-204-G - ORDER NO. 90-1010
OCTOBER 17, 1990

IN RE: South Carolina Pipeline Corporation -) ORDER DENYING
Application for a Rate Reduction and) PETITIONS FOR
Adjustments in its Gas Rate Schedules) RECONSIDERATION,
and Tariffs and Terms and Conditions,) GRANTING STAY
and restructuring of Contracts.) AND AMENDING
) ORDER NO. 90-729

I.

INTRODUCTION

Before the Commission is a Motion for Stay and Petition for Reconsideration of the South Carolina Energy Users Committee (SCEUC) dated September 19, 1990, and a Petition for Rehearing and Reconsideration submitted by Nucor Steel Corporation (Nucor) dated September 24, 1990. Both of these documents seek reconsideration of portions of South Carolina Public Service Commission (the Commission) Order No. 90-729 dated August 8, 1990. After review of Order No. 90-729, the Commission finds that the Petitions for Reconsideration should be denied and the Order affirmed. The Commission will address within this order certain issues that were raised in the Petitions. The Commission also grants the Stay requested by the SCEUC for the reasons set forth within this order.

II.

THE PETITION OF THE SCEUC

1. Paragraphs 8 and 10 of the SCEUC's Petition for Reconsideration

Paragraph 8 of the SCEUC's petition alleges that "[i]n allowing South Carolina Pipeline to make adjustment to the Weighted Average Cost of Gas by way of demand and commodity charge manipulation, the Order unlawfully contravenes South Carolina Code Ann., §1-23-380(g)." This allegation does not specify what "demand and commodity charge manipulation" is or how it could be permitted under the Order. The Commission has reviewed the Order. The Commission finds nothing in it that authorizes "demand and commodity charge manipulation." There is no evidence in the record indicating that demand and commodity charge manipulation is threatened. If any such threat exists, the allegation in the Petition for Rehearing is inadequate to direct the Commission's attention to it.

In Paragraph 10 the allegation is made that the order does not contain adequate findings of fact or conclusions of law. This paragraph does not specify the issue or issues on which adequate findings are absent. The Commission has reviewed all rulings challenged in the petition and has determined that there are sufficient findings of fact and conclusions of law on each issue in dispute.

2. Paragraphs 5, 6 and 7 of the SCEUC's Petition

Paragraphs 5, 6 and 7 of the SCEUC's petition allege that the Commission failed to make findings of fact related to the Pipeline's fair or actual rate of return, specifically as regards Pipeline's industrial operations or overall operations including industrial operations. In each case, the SCEUC asserts that the Commission was required to establish returns based on cost of service principles.

Order No. 90-729 discusses at length why cost of service based regulation was not adopted for Pipeline's industrial operations in this case. Therefore, cost of service return figures for those operations, either separately or in combination with other operations, are not figures which are relevant to the issues decided in the order.

3. Paragraph 9 of the SCEUC's Petition

In paragraph 9 of their petition, the SCEUC alleges that the Commission erred in setting a subsequent hearing to address maximum rate caps because "such evidence should have been submitted on the record and not at a subsequent hearing." This allegation, however, does not suggest that evidence concerning maximum rate caps would have been material to any issue decided in the Order. As the Order reflects, maximum rate caps were not an issue before the Commission. No party proposed any change in those caps. The Commission, at its own instance, decided that it would be advisable

to review the rate caps and opened a separate docket to do so. Evidence related to rate caps was not necessary to determine any issue addressed in Order No. 90-729.

III.

MOTION FOR STAY

The SCEUC filed a Motion for a Stay of that portion of Order No. 90-279 which orders a hearing on maximum rate levels. The principal basis for this motion is that a hearing would be premature until judicial review of Order No. 90-279 is completed. On that basis, the Commission finds that a stay of that portion of Order No. 90-279 should be granted.

The Commission will continue the proceedings in Docket No. 90-588-G, pending resolution of the judicial review of this Order.

IV.

PETITION FOR REHEARING BY NUCOR

1. Ratemaking Methodology

Nucor asserts that the Commission's failure to adopt cost of service based ratemaking represents a failure by the Commission to discharge its duty to regulate Pipeline.

As Order No. 90-729 shows, Pipeline's industrial sales are made in competitive markets. Accordingly, the Commission has determined that it is appropriate for industrial sales margins to be set competitively. The Commission has stated that competition in industrial fuels markets--as reflected in negotiated contracts--is an appropriate means for setting industrial margins.

The decision to allow margins to be determined through competition and negotiation is an affirmative regulatory decision by the Commission. It does not constitute an abandonment of regulatory power or supervision over Pipeline. Pipeline is allowed to negotiate with its industrial customers as to contract margins. But each industrial contract is filed with the Commission. Furthermore, the maximum margin under each industrial contract is set according to the maximum margin caps discussed above.

In addition, the vast majority of industrial sales are made at competitive prices under the industrial sales program rider or ISPR program. The ISPR program is a Commission approved sales program of general applicability. Sales under this program are reviewed on an annual basis by the Commission.

Order No. 90-729 discusses at length the reasons why South Carolina Pipeline Corporation is allowed to charge negotiated rates in its industrial market. In fact, this has been established as the Commission's regulatory policy since 1957.

The fact that negotiated rates do not reflect strict cost of service principles does not mean that the Commission is not carrying out its regulatory responsibilities under State law. Pricing a utility service involves setting rates for each class of service based on many variables, including required investment, load factor, customer costs, availability of supply, value of service, and consistency with past pricing methods. Utility ratemaking is not an exact science. The negotiated ratemaking process approved by the Commission is a blend of these recognized

ingredients of ratemaking. The negotiated process even goes one step further. It allows for the customer to bargain the price downward. The setting of rates for a gas utility should not be envisioned as merely scrutiny of extensive cost studies to determine rates. Instead, the Commission must be concerned with other factors, as necessary, to reflect changes in economic, regulatory, supply, marketing, social and other factors as they arise from time to time.

Nucor's allegation that the Commission is not "regulating" Pipeline's industrial sales is in fact merely a dispute as to what methodology should be used for regulating margins on those sales. Nucor asserts that cost of service methodology is the only methodology that the Commission can use to regulate Pipeline's industrial sales. But as discussed in Order No. 90-729, the Commission is not obligated to use a cost of service methodology. The failure to use the methodology does not constitute a failure to regulate.

2. The "Non-Compensatory" Nature of the Utility's Rates

Nucor argues that South Carolina Pipeline's rates are "non-compensatory" because, on the average, negotiated industrial rates are higher than rates that would be set with cost of service methodology. In making this argument, Nucor assumes that the only "fair" rate is a cost of service rate and that a negotiated rate is "unfair" to the extent that it differs from rates that would be set using cost of service principles.

Nucor correctly focuses on the standard found in Mims v. Edgefield County Water & Sewer Authority, 278 S.C. 554, 556, 299 S.E.2d 484 (1983), that a rate is unreasonable where it is "so high as to be unduly burdensome to the utility's customers." Rates set by competition among industrial fuels are not unduly burdensome. In any case where gas is not available at a reasonable rate in comparison to the other fuels available on the market, industrial customers can switch to alternative fuels. The reasonableness of Pipeline's rates to industrial customers is affected by market forces. Merely because cost of service rates might produce lower rates under present market conditions does not mean that fairness requires cost of service rates to be imposed.

3. Nucor's Argument that Pipeline's Markups are Preferential

Nucor argues that Pipeline's markups are preferential because curtailment categories on which maximum markups are set are not appropriate classifications upon which to base rates.

In this proceeding, no witness presented any testimony whatsoever proposing changes in curtailment categories or asserting that curtailment categories are not an appropriate classification on which to base maximum markups. This issue is raised for the first time in Nucor's Petition. This is procedurally inappropriate and is adequate grounds for the Commission not to consider the allegation at all. Furthermore, there is not any evidence in the record that would support any change in those curtailments or in the categories by which maximum markups are set.

Pipeline's curtailment categories have been imposed in prior proceedings based on the Commission's determination of the social utility of gas service to a particular end use customer. Determinations as to social utility are an entirely appropriate basis on which to set caps; under this approach, the degree of latitude in setting margins properly tracks the utility of the service to the customer.

Nucor also alleges that there is no credible basis for charging Pipeline's industrial customers more for gas service than resale customers. As a general matter, industrial customers, because they have alternative fuel capabilities, can swing on and off Pipeline's system as their interests require. As a result, they operate under a very different set of circumstances than sale for resale customers. One result of this difference is that they represent a riskier market than sale for resale markets.

Furthermore, Pipeline's industrial customers, unlike other customers, have clauses in their contracts which allow their prices to be set purely by competitive forces. Those clauses allow Pipeline to set aside the base rate price, and reduce margins, when necessary to meet a customer's competitive fuel cost. As the record indicates, a substantial portion of Pipeline's total industrial sales are made as competitive fuel clause sales at rates below the allowed maximum rates.

Looking at maximum margin alone, resale purchasers may appear to receive lower rates on their residential and commercial purchases. But these purchasers, unlike industrial purchasers,

cannot get the benefit of these special, competitively based sales available to industrial customers. Pipeline's industrial customers are allowed to benefit from competitive pressures in alternative fuels markets when those pressures require lower gas prices.

4. Past Practices

Nucor contends that the Commission's 30 year history of allowing Pipeline to deal with its industrial customers on a value of service basis is not entitled to any weight in the decision between negotiated rates and cost of service ratemaking. The Commission disagrees.

For the past 30 years, the Commission has followed a consistent policy of allowing Pipeline to contract with industrial customers on a negotiated rate basis. During this period, Pipeline has been able to conduct its operations and arrange its finances within a consistent and stable regulatory framework. Stability and certainty in regulation are not the only values that the Commission should consider in its regulation of utilities. But they are nonetheless values worthy of consideration by this Commission in making ratemaking decisions.

5. Burden Shifting

In a related argument, Nucor asserts that the Commission has unfairly shifted the burden of persuasion to it as to industrial rates. This is incorrect. The Order states, quite properly, that a party which proposes a departure from a longstanding regulatory practice must provide the Commission with an appropriate factual and legal basis to rule in its favor.

Nucor admits that in proposing different rates for Pipeline it bears, at minimum, the burden of making out a prima facie case opposing the utility's rates. The Commission agrees with Nucor. The Commission's position on this issue is that Pipeline, as to the issues raised by Nucor as well as the other Intervenor, met its burden of persuasion once the issues were properly raised and addressed by Nucor and the other Intervenor.

6. Negotiated Rates

In its Petition for Reconsideration, Nucor asserts that of all South Carolina utilities, only South Carolina Pipeline's natural gas operations do not use cost of service rates. However, no other gas utilities under this Commission's jurisdiction have rates which are strictly based on cost of service. Cost of service is merely a guide that the Commission can use in setting gas rates.

7. Discriminatory Rates

In its Petition for Reconsideration, Nucor asserts that there was "[o]verwhelming evidence...showing that the maximum markups used by SCPC were discriminatory." The Commission has reviewed the citations to the transcript of record which Nucor makes in support of that proposition. None of the witnesses cited mentioned maximum markups at all. In fact, as the Commission mentioned earlier, while a number of parties argued for cost of service ratemaking, no party raised a challenge to any specific aspect of the present system, classifications or level of caps. There is not a sufficient factual basis in this record for the Commission to revise caps. It is for that reason that the Commission opened

Docket No. 90-588-G. Any revisions to the system of caps, so long as it is consistent with the decisions in Order No. 90-729, can be considered in that proceeding.

If Nucor's argument is that the maximum markups were discriminatory because they were not based on cost of service, then Nucor's argument has no merit. As stated numerous times in Order No. 90-729 and in this Order, rates do not have to be based on cost of service.

8. Cost of Service Based Natural Gas Transportation Rates

As the Commission found in its initial Order, South Carolina Pipeline Corporation's industrial sales are sales made in a competitive market. That relevant market for Pipeline's industrial sales is the market for industrial fuels. Natural gas is but one of many fuels that compete in that market.

The fact that Pipeline is the only supplier of one of the products that competes in that market does not make Pipeline a monopoly supplier in that market as Nucor suggests. Nor does a competitive industrial fuels market require the Commission to order cost based rates for the transportation of natural gas. Competition exists in that market as presently structured. The high volume of competitive fuels clause sales made by Pipeline is ample evidence of that fact.

The Commission's position is that transportation should be made available on a revenue neutral basis. To adopt any other approach to industrial transportation would be to place Pipeline's

merchant function in jeopardy. There are substantial reasons for not doing so.

Since its inception, Pipeline has been first and foremost a merchant of gas. It is regulated as a supplier of natural gas, not a common carrier of natural gas. As a supplier and merchant, Pipeline aggregates the demand of many customers so that it can efficiently participate in national markets as a sophisticated, high-volume buyer of gas. To erode Pipeline's merchant function could be detrimental to the State as a whole, particularly the smallest customers of Pipeline and its sale for resale customers who do not have the market power or resources necessary to effectively compete in national gas markets.

The Commission must balance the benefits to industrial customers from cost of service based transportation rates against the potential detriment to Pipeline and its other customers if such a service were imposed. The Commission has weighed the risks and benefits from Nucor's proposal and finds that on balance, the risks of cost of service based transportation outweigh the benefits to the industrial class at this time.

9. Benefits to Sale for Resale Customers

Nucor requests rehearing on the Commission's finding that negotiated rates benefit sale for resale customers. Nucor argues that this finding should be reviewed because "it is likely that the approach adopted in this proceeding will be detrimental to such customers in the future due to lost industrial sales and higher sale for resale rates." The Commission disagrees with this

assertion. As stated in Order No. 90-729, negotiated industrial rates gives Pipeline maximum flexibility to respond to changing market conditions and maintain industrial load.

10. The Acquisition Adjustment and Overall Revenue Requirements

Like the SCEUC, Nucor seeks rehearing on the question of whether the Commission was required to make express findings in its order concerning the acquisition adjustment and the establishment of overall revenue requirements based on reasonable rates of return. Nucor asserts that these findings were required by §58-5-240(h) of the Code of Laws of South Carolina.

The Commission, in Order No. 90-729, has dealt at length with the meaning and intent of §58-5-240(h). The Commission stands by its determination that §58-5-240(H) does not require cost of service principles to be used in every case. Findings on the acquisition adjustment, overall revenue requirements and reasonable rates of return are not required to support the Commission's order in this case.

11. Open Access

Nucor asserts that the Commission must require Pipeline to become an open access pipeline to ensure that industrial fuel markets are competitive. The Commission disagrees. The relevant competition in industrial fuel markets is competition between natural gas and many other fuels. Open access is not required for such competition to continue.

In Order No. 90-729, the Commission has discussed the reasons for not ordering Pipeline to become an open access pipeline. Presently, there is no problem with access on Pipeline's system. The need for mandatory open access is hypothetical. Order No. 90-729 expresses the Commission's concern as to the impact on the firm customers if Pipeline is denied the flexibility to manage transportation on its system at all times. There was no evidence offered by any party as to the effects on the firm customers if the company were ordered to provide open access interruptible transportation service. The Commission must know what these effects would be in order to protect service to the high priority residential and commercial customers in the State.

12. Nucor's Petition for Postponement

On April 24, 1990, Nucor filed its Motion to Create a Separate Docket or, in the Alternative, to Postpone Hearing. Nucor sought to delay the proceeding on the grounds that Nucor and potential concerned industrial customers did not have adequate notice and a fair opportunity to prepare for the hearing on the industrial rate issues raised by pre-filed testimony. Nucor alleges that the Commission's denial of its Motion was error. Nucor filed its Petition to Intervene within a month of the filing of Pipeline's Application and approximately a month before the hearing. It appears from Nucor's Petition to Intervene that it did have notice that industrial rate issues could be addressed in the hearing. "Based on our initial limited review, SCPC does not appear to propose any changes to its rates for industrial customers such as

Nucor. However, other parties may make proposals that will affect industrial rates."

Nucor's motion for continuance was not filed in time to be posted for consideration before the date of hearing. When confronted with Nucor's motion for continuance, the Commission weighed the possible prejudice to Nucor and other industrial customers by denying a continuance against the possible prejudice to other parties by delaying a proceeding which was otherwise ready to go forward. The Commission found, on balance, that orderly regulatory procedure favored proceeding with the hearing.

Nucor now asserts that postponement was necessary for it to prepare to argue against Pipeline's caps. Nucor, however, did not raise any issue regarding caps at the hearing. The issue as to whether Pipeline's rates should be set on a cost of service or negotiated rate basis was fully argued by the parties at the hearing. That issue has been resolved by the Commission. The Commission will review any other questions related to caps in docket 90-588-G. For reasons of administrative economy, the Commission intends not to revisit its question concerning negotiated rates versus cost of service rates in that subsequent proceeding.

13. Adequacy of Findings and Evidence

Nucor asserts that Order No. 90-729 does not contain adequate findings of fact and that there is not evidence on the record to support the Commission's decision. The Commission has reviewed the

Order and the evidence. It finds that both are completely sufficient to support the result reached.

V.

Amendment to Order No. 90-729

The Commission, upon review of Order No. 90-729, found that the Order should be amended to change the word "include" in Item No. 22 of the ordering paragraph to "exclude."

VI.

CONCLUSION

The Commission has reviewed the Petitions for Reconsideration and determines that they should be denied and Order No. 90-729 should be affirmed. The Petition for Stay is granted and the hearing scheduled in Docket No. 90-588-G will be continued until further notice. Order No. 90-729 is amended as set forth above.

BY ORDER OF THE COMMISSION:


Chairman

ATTEST:


Deputy Executive Director

(SEAL)